San Francisco Health Service System
Health Service Board

Legislative and Excise Tax Update

December 14, 2017

Prepared by:
Aon | Health & Benefits

Empower Results®

A Quick History of ACA Repeal & Replace Efforts

The House of Representatives

- 240 Republicans
- 194 Democrats
- 1 Vacancy

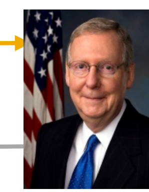
The Senate

- 52 Republicans
- 46 Democrats
- 2 Independents

Paul Ryan (R-WI)
Speaker of the House

House passed AHCA 217 to 213, but…

… Senate could not pass AHCA, BCRA, “Skinny Repeal,” or Graham-Cassidy



Mitch McConnell (R-KY)
Senate Majority Leader

Congress and the ACA Today

- **ACA remains "the law of the land," but issue remains alive in Congress**
  — Republicans claim repeal will happen in 2018, but Democrats say effort has failed
  — Window generally has closed to pass repeal with simple majority in the Senate

Senate HELP committee legislation

Graham-Cassidy

Sanders "Medicare for All" bill

U.S. House of Representatives [Tax Reform]

U.S. Senate [Tax Reform]

Congress and the ACA—Tax Reform (House)

- **H.R. 1 Tax Cuts & Jobs Act**
  - — Passed the House on November 16, 2017 on a 227-205 vote
  - — Preserves:
    - The income tax exclusion for employer-provided health care contributions and benefits
    - Individual mandate penalty (but “in-play” to be repealed by Senate) under the ACA
    - Employer mandate penalty under the ACA
    - Other ACA taxes, including the Cadillac tax (or “Excise Tax”)
    - The employer income tax deduction for the following benefits (unless such benefits are treated as taxable employee compensation or as gross income of a nonemployee recipient):
      - – On-site athletic centers
      - – Qualified transportation fringe benefits

Congress and the ACA—Tax Reform (House)

- **H.R. 1 Tax Cuts & Jobs Act (continued)**
  - Proposed changes to health and welfare benefits:
    - Eliminates dependent care flexible spending accounts (after 2022)
    - Employee income tax exclusions after 2017 for:
      - Adoption assistance programs
      - Qualified moving expenses
      - Employer-provided educational assistance programs

Congress and the ACA—Tax Reform (Senate)

- **Senate “Tax Cuts and Jobs Act”**
  - — Passed the Senate on December 2, 2017 on a 52-48 vote
  - — The act would:
    - Repeal the Affordable Care Act’s penalty on individual taxpayers who do not maintain health insurance coverage during the year beginning after December 31, 2018
    - Repeals the income tax exclusion for qualified bicycle commuting reimbursements
    - Denies employer deductions for employee transportation fringe benefits (e.g., parking and mass transit)
    - Retains the income exclusion for benefits received by an employee
    - Allow eligible employers to claim a general business credit for wages paid to qualifying employees during any period in which such employees are on Family Medical Leave Act (FMLA) leave

Congress and the ACA—Tax Reform (Senate)

- **Senate "Tax Cuts and Jobs Act" <u>would not change</u>:**
  - — The employer mandate reporting rules under the ACA;
  - — The taxes imposed under the ACA (e.g., Cadillac tax or Excise tax; net investment tax; health insurer tax; medical device tax; PCORI fee);
  - — The tax rules governing health savings accounts and health care flexible spending accounts; or
  - — The income tax exclusion for employer-provided health care contributions and benefits.
- **From here, two alternatives exist for House of Representatives:**
  - — Pass the Senate "Tax Cuts and Jobs Act" as is
  - — Engage in reconciliation of House and Senate bills

Congress and the ACA—Medicare for All Act

- **Senator Bernie Sanders introduced Medicare for All Act**
  - — Institutes single payer health care in United States
  - — Provides a comprehensive set of benefits
  - — Prohibits employer health coverage that duplicates Medicare coverage
  - — Permits secondary, non-duplicative coverage

(See Appendix for graphic example of rollout)

Trump Administration and the ACA—October 12, 2017 Executive Order

- **President Trump signed executive order telling Department of Labor (DOL), Health & Human Services (HHS), and Internal Revenue Service (IRS) to relax and reverse ACA rules on:**
  - **Health Reimbursement Arrangements (HRAs).** Order directs agencies to permit use of HRAs to purchase individual health insurance policies
    - Under current ACA rules:
      - HRAs for active employees can only be used to purchase group health coverage (and that coverage must meet certain requirements, such as integration)
      - Cannot be used to purchase individual health insurance policies sold on ACA exchanges or in individual health insurance market

Trump Administration and the ACA—October 12, 2017 Executive Order

- **President Trump signed executive order telling Department of Labor (DOL), Health & Human Services (HHS), and Internal Revenue Service (IRS) to relax and reverse ACA rules on:**
  - **Association Health Plans (AHPs)**. Order would permit small businesses in same line of business to purchase AHPs across state lines
  - **Short-Term Limited Duration (STLD) Medical Insurance**. Order would permit sale of renewable STLD medical insurance policies for coverage periods longer than three months
    - Obama Administration had limited STLD policies to three months
    - Policyholders would not be subject to individual mandate penalty

Trump Administration and the ACA—Marketplace Impact

- **Ending the Cost Sharing Reduction (CSR) Payments and Scaling Back Outreach**
  - — Trump Administration **discontinued** ACA CSR payments to insurers, stating that CSR payments were illegal because Congress had not appropriated funds
  - — Obama Administration had been making CSR payments since 2013, but in 2014, the U.S. House of Representatives sued the Obama Administration to stop CSR payments. In 2016, Federal court ruled against Obama Administration in *House v. Burwell*
  - — Enrollment in public exchanges (Nov. 1 to Dec. 15)
    - Trump Administration scaled back ACA outreach efforts for enrollment: ACA advertising budget reduced from $100M to $10M and ACA navigator funding reduced from $65M to $37M
    - Almost 2.3 million signed up through healthcare.gov so far (excluding enrollment from state-run marketplaces)

Trump Administration and the ACA—Individual & Employer Mandates

- **Enforcing the Individual Shared Responsibility Mandate**
  - Trump Administration has suggested that it might be less than diligent in enforcing the ACA's individual mandate
    - ACA executive order in January 2017 directed the agencies, including the IRS and Treasury, to reduce the ACA's burdens
  - **Individual Mandate and Tax Forms.** IRS has ***now*** announced that income tax forms will **<u>not</u>** be processed unless taxpayers answer question on health insurance coverage
  - Any lack of enforcement of individual mandate will adversely affect:
    - Insurer participation in public exchanges
    - Premium costs in public exchanges

(See Appendix for more details)

Employers and the ACA

- **Group Market Reforms Remain in Effect**
  - — Employers should have documentation with health plan administrator/insurer that group market reforms remain up to date on behalf of employer
  - — Employers should communicate the group market reforms in Summary Plan Description (SPD) and updates in annual enrollment materials via Summary of Material Modification (SMM)
  - — Group market reforms include (but are not limited to):
    - ACA's prohibition against annual/lifetime ***dollar limits*** on essential health benefits
    - **Summaries of Benefits and Coverage (SBC)**—changes for 2018!
    - **Extension of coverage to age 26 for adult children**
      - – Note: HMOs cannot restrict coverage to adult children based on where they live

Employers and the ACA (continued)

- **Group Market Reforms Remain in Effect**
  - Group market reforms include (but are not limited to):
    - **Changes to ERISA claims and appeals rules** (non-grandfathered plans) including Independent Review Organizations (IRO)
    - **Out-of-pocket expense maximum limits** (non-grandfathered plans): $7,350 (individual) and $14,700 (family) (2018)
    - **In-network preventive care without cost sharing** (non-grandfathered plans) difficult to maintain because it changes annually – for example:
      - Screenings (e.g., blood pressure, cholesterol, obesity)
      - Colonoscopies and many related procedures
      - Many contraception requirements
      - Coverage of statins for adults that meet specific criteria (generally ages 40 to 75 years with specific risk factors)

Employers and the ACA (continued)

- **Health Insurer Fee Starts Up Again in 2018**
  - — The collapse of "repeal and replace" means that the ACA's taxes remain on the books
    - Includes the health insurer fee, which is paid by health insurance issuers and HMOs
    - Health insurer fee was suspended for 2017 but becomes effective again in 2018
- **Patient Centered Outcomes Research Institute (PCORI) Fee Remains on the Books**
  - — For self-funded plans, employers remain liable for payment of the PCORI fee, which expires with the plan year ending before October 1, 2019 ($2.39 per member per month for 2018)

Employers and the ACA—Cadillac Tax (or "Excise Tax")

Will Congress take action before 2020?

Bipartisan opposition

Will IRS issue guidance soon?

Notice or proposed rule anticipated in December 2017

Cadillac Tax is Imminent

2020

Employers should prepare:

Modeling
Union agreements

Guidance Needed:

How to calculate tax?

Which entity pays? TPA? Employer? Insurer?

Excise Tax—As written in the ACA (March 2010)

Starting in 2018, insurers (including employers for self-insured plans) pay a 40% excise tax on the aggregate value of the portion of employer-sponsored insurance in excess of thresholds

- Thresholds for actives and post-Medicare retirees are:
  - $10,200 for single coverage
  - $27,500 for family coverage
  - Thresholds indexed at CPI-U (assumed to be 2.2%)
    - The threshold is indexed with an additional 1% in 2019
  - $1,650 / $3,450 for "qualified retirees" (pre-65 retirees) and high risk professions/installation of electrical or telecommunications lines
  - Additional adjustments may be made based on age and gender demographics of the population

Excise Tax—As written in the ACA (March 2010)

Starting in 2018, insurers (including employers for self-insured plans) pay a 40% excise tax on the aggregate value of the portion of employer-sponsored insurance in excess of thresholds

— Coverage subject to tax includes employer contributions and employee pre-tax contributions under cafeteria plans
  - Medical Coverage
  - Employer Contributions to Health Reimbursement Arrangement (HRA)
  - Employee Pre-Tax Contributions to Health Savings Account (HSA) and Flexible Spending Account (FSA) plans
  - Dental and Vision are also subject to the tax if the respective plan is self-insured or bundled with Medical coverage (under current guidance)

— Excise Tax is not tax-deductible

Excise Tax—December 2015 Legislative Update

- Effective December 18, 2015, the President signed into law a significant tax cut and spending package that avoids a government shutdown and funds federal agencies through Fall 2016. The new law contains provisions which impact the ACA excise tax on high-cost group health plans. These provisions include:
  - Delay implementation of excise tax for 2 years – from 2018 to 2020;
  - Allow the excise tax to be deductible to the taxpayer (generally the insurance carrier or third party claims administrator); and
  - Commission a study on the appropriateness of using the Federal Health Benefits Plan as a benchmark for the age and gender adjustment of the applicable dollar limit for the excise tax.
- Under current CPI-U indexing assumptions, the thresholds in 2020 are:
  - $10,758 for single coverage
  - $29,004 for family coverage

Excise Tax—Analysis

- The ACA does outline an option to blend "similarly situated" Pre-Medicare and Medicare retirees. This has been interpreted and applied by creating a composite premium for all retirees—blending Pre-Medicare and Medicare premiums by enrollment
- Applying a reasonable interpretation of blending Pre-Medicare and Medicare Retiree rates produces the results on slide 25
- This analysis assumes an additional adjustment to the thresholds shown above based on the demographics of the SFHSS membership modeled against the National Workforce

Excise Tax Analysis—Results

			2020 Estimated Coverage Cost				Excise Tax	
Option Name	**Status**	**Tier**	**Estimated Enrollment**	**Cost Per Enrolled Member**	**Aggregate Plan Cost**	**Year Crossing Threshold**	**Estimated Excise Tax in 2020**	**10 Year PV of Estimated Excise Tax**
City Plan Actives	Active	Single Family	660 352	$ 12,344 $ 28,365	$18,100,000	2023 2025	$ 0	$6,870,000
City Plan Pre-65	Pre-65	Single Family	554 178	$ 5,960 $ 14,237	$5,840,000	2040 2042	$ 0	$ 0
UHC Medicare Advantage PPO	Post-65	Single Family	9,051 2,959	$ 5,960 $ 11,847	$89,000,000	2038 2044	$ 0	$ 0
Blue Shield Actives	Active	Single Family	6,818 8,604	$ 11,021 $ 26,633	$304,000,000	2025 2026	$ 0	$53,500,000
Blue Shield Pre-65	Pre-65	Single Family	1,920 833	$ 25,477 $ 39,157	$81,500,000	2020 2021	$7,550,000	$130,000,000
Kaiser Actives	Active	Single Family	11,738 12,251	$ 8,546 $ 20,695	$354,000,000	2030 2031	$ 0	$ 0
Kaiser Pre-65	Pre-65	Single Family	1,801 880	$ 7,713 $ 15,772	$27,800,000	2035 2039	$ 0	$ 0
Kaiser Post-65	Post-65	Single Family	7,138 2,977	$ 7,713 $ 14,124	$97,100,000	2032 2040	$ 0	$ 0
TOTAL			**68,714**		**$977,340,000**		**$7,550,000**	**$190,370,000**

Notes:

- This calculation is for illustrative purposes only. The excise tax estimates are subject to change, pending guidance and regulations.
- Assumptions are detailed in the Appendix.

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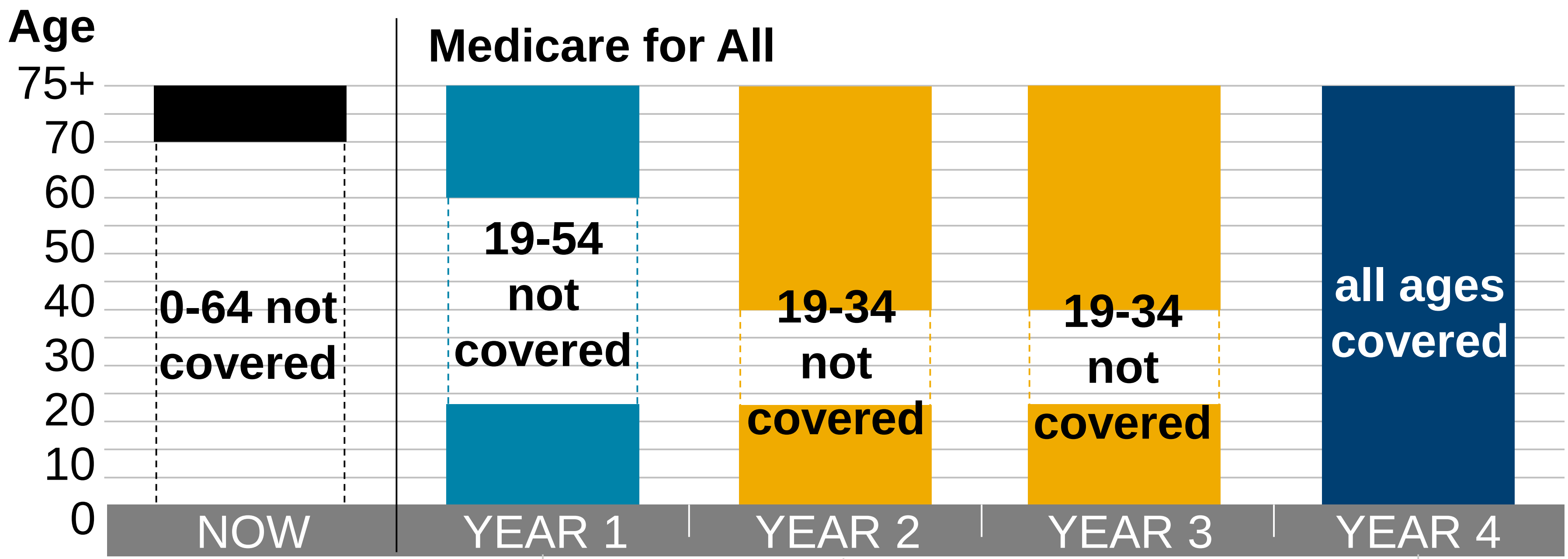
Excise Tax—Observations

- San Francisco Health Service System's (SFHSS) medical plans are expected to incur $7,550,000 in excise tax liabilities in 2020
  - Only the BlueShield HMO is expected to cross the excise tax threshold in 2020 for single pre-65 retirees
  - Blending produces savings of $1,318,000 in excise tax liability in 2020
- Trend assumptions follow Aon's internal trend guidance levels for years 2018 through 2020.Trend assumptions after 2020 decrease by 0.25% per year until they hit a minimum of 4.50% for each of medical and prescription drug.
- Medicare Advantage was moved to UHC effective January 1, 2017. Aon's methodology does not blend across carriers, resulting in unavoidable excise tax liability assessed against pre-65 retirees enrolled in BlueShield HMO.
- Due to lack of regulatory guidance, Aon does not recommend performing blending methodologies across carriers.

Acronyms

- **ACA:** Affordable Care Act
- **AHCA:** American Health Care Act
- **BCRA:** Better Care Reconciliation Act
- **CSR:** Cost-Sharing Reduction
- **DOL:** Department of Labor
- **ERISA:** Employee Retirement Income Security Act
- **HELP Committee:** Health, Education, Labor & Pensions
- **HHS:** Health & Human Services
- **IRS:** Internal Revenue Service
- **PCORI:** Patient Centered Outcomes Research Institute
- **TPA:** Third-party Administrator

Congress and the ACA—Medicare for All Act



Eligibility age for Medicare would be lowered to 55

All children under age 18 would be covered

Eligibility age would be lowered from 55 to 35

Every American would be covered by Medicare for All

Trump Administration and the ACA—Individual & Employer Mandates

- **Enforcing the Employer Shared Responsibility (ESR) Mandate**
  - — **Employer Mandate (New!)** IRS FAQs issued in early November 2017 indicate that employer mandate collection will begin soon
  - — IRS will send **Letter 226J** to an employer if IRS determines at least one full-time employee (FTE) received premium tax credit for ACA exchange plan for at least one month
    - Notifies employer of proposed ESR payment
    - Contains ESR payment response **Form 14764**
    - **Form 14765** lists full-time employees for whom ESR payment is assessed

Trump Administration and the ACA—Individual & Employer Mandates

- **Enforcing the Employer Shared Responsibility (ESR) Mandate**
  - Employer response to Letter 226J
    - Due within 30 days
    - IRS follows up with **Letter 227** and possible conference with IRS (name of specific IRS employee to contact will be included)
  - Opportunity to appeal – instructions available
  - IRS issues **Notice CP 220J** if IRS determines employer is liable for ESR payment

Excise Tax—Thresholds

- For active employees and post-65 retirees, the 2020 thresholds used for this calculation were $13,905 for individual coverage and $36,300 for family coverage
- For pre-65 retirees, the 2020 thresholds used for this calculation were $15,646 for individual coverage and $39,938 for family coverage
- Thresholds above include age / sex factor adjustments
- Thresholds for pre-65 and post-65 retirees were not blended for this analysis

Excise Tax—Assumptions

- Non-single coverage combined and underwritten as family ("other than self-only coverage")
- Pre-Tax equivalent assumes that the medical vendors will be assess a 0% tax liability on the penalty which may be passed to the plan sponsor
- Present value calculation of the Excise Tax assumes 5.00% discount rate, and reflects the present value of the excise tax from 2020 - 2029 as of 1/1/2018
- Estimated costs include the following expenses: medical and prescription drugs
- Plan costs are estimated by trending 2018 premium equivalent rates
- Assumed no plan design, network, or other changes affecting expected costs (besides trend) between 2018 and 2020
- Enrollment and Rates based on 2018 information
- Fully-insured Vision premium has not been included
- Rates for UHC and Kaiser’s pre-65 and post-65 retiree populations were blended by enrollment and per carrier

Legal Disclaimer

The information in this presentation is not intended to be legal advice.
As always, Aon is not in the practice of law